

## Behind the Counter

### Financing Options for your business

This begins a three part discussion on financing and will be relevant whether you are just starting a business or need financing for an existing business and whether your business is a small home based business or a larger corporation.

The sources of financing have evolved over the years and we now have several sources of financing from individual family members, banks and insurance companies to investment funds and venture capital companies.

There are several reasons why companies need financing. Some are – start up capital, additional working capital, purchase of machinery and equipment, purchase of real estate, purchase of a business or reorganization of a business. Once you determine why you need the financing, then you can determine which organization to approach to apply for financing as not all organizations will lend you money for every purpose.

The reason for financing will also help you determine the terms of the financing. For example, if you require funds to finance increasing sales – that would be short term financing as the resulting sales should be sufficient to pay that back in the short term. If you are financing an asset, then the asset life should at least be long enough to equal the term of the loan. If you are starting your business, purchasing a business, or purchasing real estate, that would probably require a long term loan.

Short term funds would be financed with demand notes or loans of one year or less.

Medium term financing usually means repayment in one to five years and long term financing will be over five or more years.

The next question to answer is – How much do I actually need? If your purpose is the purchase of equipment, the answer to that question is pretty straightforward as it should be enough to cover the purchase price of the equipment and that piece of equipment should generate enough cash to cover the loan payment. However, if you are wishing to finance working capital or business start up, the answer is not as clear. You would want to make sure that you get enough financing, but not too much so that you are strapped from doing anything else due to a heavy debt load.

There is the story of the company that financed a piece of heavy duty equipment and the lending institution that provided the financing required that the debt to equity ratio be kept at 1:2. Word got out to their customers that they had acquired this new piece of equipment, so they were asked to complete some pretty large lucrative contracts however, they did not have the working capital to purchase the raw material required for the contracts. They went back to the lending institution to get more financing and were turned down. They approached another institution for the funds and were accepted. Unfortunately, this new loan changed the debt to equity ratio to be 1:1, so the first lending institution called the first loan. Then the company had to scramble for some alternate higher rate financing to replace that first loan or lose the new sales contracts and go under.

From a tax perspective, any interest that you pay on a loan to finance your business is tax deductible in your business as are any fees that you incur to set up the financing agreement.

If you have an existing company, perhaps changing some of the internal cash management procedures might be enough to get you the extra cash that you might need without needing to go to an external funding source. An example would be to change the terms of accounts receivable collections. If your terms are currently Net 30, perhaps changing them to Net 15 or adding a discount for early payment might speed up the cash flow. You can also change the way that accounts payable are paid by taking advantage of all discounts and pay payables on the day before they would incur interest charges. Keeping track of this on a manual system is extremely time consuming, but most of the current accounting computer systems will allow you set up your customer and vendor accounts individually to take control of your cash flow issues.

The next issue of this column will discuss the external sources of financing.

**Hot Tax Tip** I just received an email from the Canada Revenue Agency about some Email Fraud. Many people have been getting emails that say or appear to say that the email is from the Canada Revenue Agency (CRA) confirming the registration of a complaint case. This email is not from the CRA. The web links inside the email contain harmful software. If you receive this email, delete it – do not open it.

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